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STATE PLEASE PASS TO USTR KATE KALUTKIEWICZ  
STATE PLEASE PASS TO FEDERAL RESERVE TOM CONNORS  
TREASURY FOR BLINDQUIST  
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SUBJECT: CHILE'S ECONOMIC HIGHLIGHTS - END OF 2009

REF: 09 SANTIAGO 1074

**¶1. SUMMARY:** Chile has finally emerged from its recession. The economy showed concrete signs of recovery at the end of 2009 as economic activity expanded in November and December for the first time in nine months. Economists estimate the Chilean economy shrank by 1.7% in 2009, however, GDP is expected to grow by 4.5 - 5.5% in 2010. The unemployment rate fell four months in a row to 8.6% in December, bringing estimates for 2009's average unemployment rate to 9.7%. Deflation continued, with a drop of 0.5% in November and 0.3% in December bringing annualized inflation for 2009 to -1.4%. Chile's Central Bank continued to keep the key interest rate at its minimum level of 0.5% in November and December. Trade numbers were significantly lower in 2009, and Chile ran a trade deficit with the U.S. during the year. The GOC budget deficit increased as did Chile's foreign debt. Copper prices increased 150% in 2009, the Peso appreciated against the Dollar by 20% for the year, and the stock market index rose by 51% in 2009. END SUMMARY.

Recession Ends but Economy Contracts Slightly in 2009

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**¶2.** Building on recent, tentative signs of a recovery, Chile can now point to concrete numbers that demonstrate it has emerged from its recession. The Central Bank reported that the monthly economic activity indicator (Imacec) grew by 3.1% in November 2009 compared with the same month in 2008. This was the first month of growth after 12 months of contraction. The trend continued with a greater than expected 3.9% expansion in the Imacec in December. Experts had been hoping for positive year-on-year Imacec numbers since the beginning of the fourth quarter of 2009. Based on this data, the Central Bank will likely determine that Chile's GDP contracted by 1.7% in 2009 (as opposed to growing 3.2% in 2008). The Central Bank predicts (and many observers agree) that Chilean GDP will grow 4.5 - 5.5% in 2010.

Unemployment Drops but Remains High for 2009

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¶3. The National Statistics Institute (INE) reported that the national unemployment rate fell to 9.7% during August - October 2009, then to 9.1% during September - November 2009, and to 8.6% during October - December 2009. The last four reports have shown a steady and significant drop in the national unemployment rate after nine straight previous increases. Based on these numbers, it is likely Chile's unemployment rate for 2009 will be 9.7% compared to 7.8% for 2008.

2009 is a Year of Deflation

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¶4. The INE also reported that the Consumer Price Index decreased 0.5% in November compared with the preceding month and fell again by 0.3% in December. This continued the trend of deflation in previous months. Chile's CPI has decreased in eight of the last 12 months in comparison with the month before. Based on these numbers, the CPI's annualized change was -1.4% for 2009 as compared to 7.1% in 2008.

Interest Rates Kept at Rock Bottom

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¶5. The Central Bank decided to maintain the key interest rate (monetary policy rate) at its minimum of 0.5% in November and again in December. This continues the policy announced previously by the Bank that the rate would remain in effect for a "prolonged" period of time, possibly until the second quarter of 2010. The Central Bank cut the rate to 0.5% in July, where it has remained for the last six months.

Trade Levels Fall in 2009; Deficit with U.S.

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¶6. According to the Central Bank, at the end of 2009, total Chilean exports (f.o.b.) were valued at \$53 billion, down by 20% compared to 2008. Total imports (f.o.b.) were valued at about \$40 billion, down by 31% in comparison with the year before. Chile's trade surplus was about 51% higher than in 2008.

¶7. A recent report, from the Ministry of Foreign Relation's General Directorate for International Economic Relations (DIRECON - the trade ministry equivalent), stated that total U.S. - Chilean trade in 2009 was valued at \$13.3 billion (about 31% lower than in 2008). Chilean exports to the U.S. were \$6 billion (a 26% drop from 2008), while its imports from the U.S. were \$7.3 billion (an almost 34% drop from 2008). The U.S. was Chile's second largest trading partner in 2009 after China.

Significant Government Deficit in 2009

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¶8. The GOC recently announced a 2009 budget deficit of \$7.2 billion (equal to 4.5% of GDP), resulting from increased public spending to stave off the effects of the global economic crisis. Cooper revenues declined 51.3% in 2009 as compared to 2008, while

spending rose 17.3%, and tax revenues fell 20.4%. According to Chile's Budget Directorate (DIPRES) this figure is Chile's biggest budget deficit since 1990. The structural deficit, using the GOC's long-term copper price forecast, was about 0.9% of GDP. [Note: Since 2001, Chilean law normally mandates a structural budget surplus of 1% of GDP. In May 2008 it was temporarily reduced to 0.5%, and this year to 0%, as a result of the economic crisis. End note.]

#### Foreign Debt Increases

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¶9. The Government of Chile's debt in 2009 totaled CHP5.3 trillion (about \$10.6 billion), or 6.3% of GDP, up from 5.2% of GDP in 2008. Chile's gross external debt reached \$74 billion by the end of 2009, up 14% from 2008. On December 31, 2009, international reserves were valued at \$25.4 billion, up about 10% from the year before. The Chilean sovereign wealth funds were valued at \$14.7 billion at the end of 2009. The two funds have posted annual returns of 6.9% since their creation in 2007.

#### Copper Prices Up 150% in 2009

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¶10. On the London Metals Exchange, copper closed at approximately \$3.33/pound on December 31, 2009. The price of copper rose by over 150% during the year.

#### Chilean Peso Appreciates Against Dollar in 2009

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¶11. On December 30, 2009, the observed exchange rate closed at approximately 506 Chilean Pesos to 1 U.S. Dollar. The Peso appreciated almost 20% against the Dollar during the year.

#### Stock Market Up Significantly for 2009

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¶12. On December 30, 2009, the last day of trading for the year, the IPSA closed at 3582.98. The IPSA ended the year up almost 51%.

¶13. The Santiago Stock Exchange will conduct its yearly update of the list of companies that make up the IPSA index. Unlike other international stock indexes, Chile calculates not only the relative weight of shares based on market capitalization (price multiplied by the number of shares), but also adjusts for the free-float. This reduces the relative weight of stock in which majority shareholders control such a large portion that the stock's liquidity is quite low. The IPSA uses the top 40 stocks with at least \$200 million in market capitalization and with the highest amounts traded in recent quarters (weighted so that the volume of the most recent quarters is greater).

¶14. Critics have claimed the IPSA index is poorly calculated. They charge that half of the trading activity in the IPSA is attributable to the stock of only six companies. There are also

claims that some of the shares included in the IPSA have low liquidity and are not representative of the national economy as a whole. For example, mining, one of Chile's top industries, is thought to be under-represented in the IPSA.

SIMONS